TRUST LAW

Trustees should fear judicial 'caprice' and 'uncertainty'

By Anthony Grant

Section 73 of the Trustee Act allows courts to relieve trustees of liability if they have acted "honestly and reasonably and ought fairly to be excused for their breaches of trust and for omitting to obtain the directions of the court..."

The words sound comforting– but don't rely on them. In *Wong v Burt* [2005] 1 NZLR 91 trustees of Trust A made a distribution of $250,000 to Mrs Wong in the expectation that she would advance the sum for the benefit of her daughter Philippa's two children who were not beneficiaries of Trust A.

Philippa had died unexpectedly at the age of 43. Had she lived, she would have received income from Trust A that would have helped her to look after the two children.

Mrs Wong believed the settlor (Mr Wong) would never have contemplated his two grandchildren would be left without financial support and he would have wanted the trustees to make the advance for their benefit.

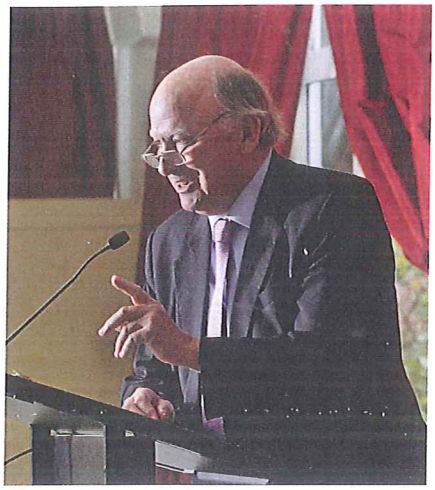
Trust A contained a broad power to benefit Mrs Wong: the trustees could make a distribution to her "for any... reason whatsoever."

There were two other trustees – an accountant and a solicitor. The trustees took advice from a major law firm which advised "there might be a challenge to the capital distribution" to Mrs Wong. The trustees weren't much disturbed by this since they were authorised to make a distribution to Mrs Wong "for any reason whatsoever..."

The trustees' decision was subsequently challenged. Ronald Young J held the payment was for Mrs Wong's benefit in that it relieved her of the moral duty she felt to her grandchildren. But if he were wrong about this, the trustees were entitled to be relieved from liability under s 73 in that they had acted honestly and reasonably, they had obtained legal and accounting advice and there had been a family emergency requiring financial support to be given for two vulnerable children.

The law in this area is unhelpfully vague. The Court of Appeal said if a distribution were made to X on the basis that he would give part of the moneys to his parents who were not beneficiaries, there would be a breach of trust. And if X were under pressure to benefit his parents, there would be a breach of trust. But if X "has genuine freedom of action and wishes to [help his parents] then there would not be a breach of trust." These propositions will be indistinguishable to most people.

As I will mention in a moment, the law has moved on a bit since then.



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The case went to the Court of Appeal where Justice Grant Hammond gave the court's decision in alarmist language. He said:

- The distribution was made deliberately to benefit non-beneficiaries.
- It was a "startling" proposition that the trustees could make the moneys available for the benefit of the grandchildren.
- He said, "acting on incorrect [legal] advice cannot... provide trustees with a shield".
- It was "downright foolish" for the trustees to have believed they could make a distribution to Mrs Wong for the purpose of benefiting her grandchildren.
- An "honest person" in Mrs Wong's position should have gone to the significant expense of seeking directions from the court.

The trustees were accordingly held liable to restore the distribution, together with interest, to the trust.

The authors of *Lewin* have not been impressed with the harshness of the Court of Appeal's approach. They say the court might have treated the trustees' claim "more seriously" if it had considered the case of *Re Hampden Settlement Trusts* [1977] TR 177.

Here, an entire trust fund had been distributed to a beneficiary for the benefit of non-beneficiaries and the court had upheld the arrangement.

The decision in *Re Hampden Settlement Trusts* was not novel: there was authority to the same effect almost 100 years before that in *Re Turner's Settled Estates* (1884) Ch D 205.

If a beneficiary has a moral obligation to a non-beneficiary, it ought not to be objectionable to make a distribution to the non-beneficiary.

The distribution is not made to benefit the non-beneficiary but to benefit the beneficiary by relieving him or her of their obligations to the non-beneficiary.

The Supreme Court has subsequently confirmed this in *Kain v Hutton* [2008] 3 NZLR 589 at [49] where it was said "an appointment which secures a benefit for a non-object is not for that reason alone a fraud on a power. The focus should rather be on whether the purpose of the appointment was truly to benefit an object. If that is so, it does not matter that a non-object also obtains a benefit."

The purpose of this article is not to record how trustees can legitimately benefit non-beneficiaries but to show the caprice that exists with the judicial process.

Ronald Young J held that the trustees were not in breach of trust in making the $250,000 available to the grandchildren but even if they were, they had acted "honestly and reasonably and ought fairly to be excused".

By contrast Anderson P, Hammond J and William Young J in the Court of Appeal unanimously said the trustees had been "downright foolish" to have done what they did and it was "startling" that they should have thought that they could get away with it.

English courts had earlier held for about 120 years that such conduct was reasonable and our Supreme Court later said such conduct was reasonable.

The lesson for trustees is to fear the uncertainty of the judicial process and to realise that despite the comfortable words of s 73, they cannot rely on the courts to relieve them of liability when they have "acted on incorrect advice", let alone when they have acted in ways that many, if not most, people would consider to have been "honest and reasonable".

Anthony Grant is an Auckland barrister specialising in trusts and estates law